COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, DECEMBER 18, 2001

APPLICATION OF

BARC ELECTRIC COOPERATIVE CASE NO. PUE010002

For approval of a functional
separation plan

FINAL ORDER

On December 29, 2000, BARC Electric Cooperative ("BARC" or the "Cooperative"), filed an application for State Corporation Commission ("Commission") approval of the Cooperative's plan for functional separation ("Plan") as required by the Virginia Electric Utility Restructuring Act ("the Act"), Chapter 23 of Title 56 of the Code of Virginia (§ 56-576 et seq.) The Act requires that the Commission complete its review of proposed plans of separation by January 1, 2002, and that transition to competition be implemented according to a timeline established by the Commission. Pursuant to an Order issued on March 30, 2001, in Case No. PUE000740, the Commission established January 1, 2004, as the deadline for BARC and other electric cooperatives to provide full retail access for their customers.

The Commission promulgated rules[1] for functional separation as required by the Act. These Rules require the Cooperative to

[1] Commission's Regulations Governing the Functional Separation of Incumbent Electric Utilities under the Virginia Electric Utility Restructuring Act ("Rules"), 20 VAC 5-202-10 et seq., adopted in Case No. PUA000029.

file a Plan that includes a cost of service study separating the Virginia jurisdictional operations into functions: generation, transmission, and distribution, subdivided by class and specifically identifying the costs associated with metering and billing. The Rules also require that the Plan include proposed unbundled rates, tariffs, and terms and conditions for service. Requests for waiver from the required submission of documents under the various sections of the Rules are also permitted.

In its application, the Cooperative stated that it is currently functionally separated. It does not own or control any generation or transmission facilities, nor does it own or control any affiliated entity that owns or controls generation or transmission facilities. Instead, BARC purchases all of its requirements for demand, energy, transmission and ancillary services through contracts with Old Dominion Electric Cooperative and Southeastern Power Administration. As such, BARC stated that it had no plans to divest itself of any generation assets, to create any new functionally separate entity, or to propose to transfer any functions, services, or employees to a functionally separate entity or third party. In its application, noting that a cost of service study had been filed with its rate application in Case No. PUE000232, the Cooperative sought a waiver of 20 VAC 5-202-40 B 7 of the Rules which requires a cost of service study to be filed with the functional separation plan. The Cooperative also requested that the Commission waive the requirement of 20 VAC 5-202-40 B 8 of the Rules to file unbundled tariff rates and terms and conditions of service with the Cooperative's functional separation plan. The Cooperative asked that the waiver extend until the conclusion of this proceeding so it can finalize and submit such filings in compliance with the final order.

In an Order dated February 5, 2001, in this proceeding, the Commission directed the Cooperative to provide notice to the public and established a procedural schedule for the filing of comments or requests for hearing on BARC's application. In that Order, the Commission directed its Staff to investigate the application and file a Report detailing its findings and recommendations.[2] The Commission directed the Cooperative to file in this proceeding the cost of service study, together with unbundled tariff rates and terms and conditions of service derived from that study, upon which it intended to rely.

On February 23, 2001, BARC filed a Motion for Clarification of the Commission's February 5, 2001, Order. The Cooperative stated that it would prepare and file its cost of service study and unbundled rate schedules as required by the March 1, 2001,

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[2] On July 3, 2001, the Commission granted a motion by Staff to extend generally the date by which Staff must file the Staff Report, as well as to extend the date by which a response must be submitted. On August 27, 2001, the Commission granted Staff's request that these dates be established as September 28, 2001, and October 12, 2001, respectively. On September 19, 2001, the Commission granted a further Staff motion extending these dates to October 19, 2001, and November 2, 2001, respectively.

deadline.[3] BARC renewed its petition for a waiver of the filing of the terms and conditions of service pending resolution of open dockets concerning the phase-in of retail competition.

On March 1, 2001, the Commission, inter alia, granted BARC's request for a waiver of 20 VAC 5-202-40 B 8 of the Rules in part. The Commission required BARC to file terms and conditions of service in time for the Commission to consider them and to require notice, if necessary and appropriate, prior to the Cooperative's implementation of retail choice to its customers.

On June 4, 2001, AES NewEnergy, Inc. ("AES") filed a Notice of Protest and request for hearing in this matter. Specifically, AES requested that a hearing schedule be established to consider issues relating to the allocation of certain costs to the generation and transmission ("G&T") functions, a dual billing option for suppliers, wires charge calculations, and the terms and conditions of service included in any rate tariff or supplier coordination agreement.

On July 16, 2001, BARC filed proof of notice and proof of publication pursuant to the Commission’s February 5, 2001, Order as amended by the Commission’s March 1, 2001, Order.

On August 1, 2001, AES filed a Motion to Withdraw its Request for Hearing.[4]

[3] On March 1, 2001, BARC made a supplemental filing with the Commission that included a revised cost of service study and unbundled rate charges.

On October 19, 2001, Staff filed its Report wherein it recommended that the Commission approve BARC's Plan with the adoption of certain modifications recommended by Staff. Specifically, Staff recommended that the Commission adopt the following: Staff's recommendation to consolidate the Cooperative's G&T functions into one function;[5] Staff's adjustments to the Cooperative's per books cost of service study; Staff's allocations of expense and rate base to the G&T function; Staff's recommendation that the Commission direct the Cooperative to track the costs associated with G&T operations; and Staff's recommendation that the Commission direct BARC to provide tariff rates and terms and conditions of service in time for full consideration by the Commission.

On November 2, 2001, BARC filed its Response to the Staff Report. In its Response, the Cooperative stated that although it supported Staff's recommendation that the G&T functions be combined, it did not agree with Staff's recommendations pertaining to functional cost assignment. BARC requested that the Commission find that its administrative and general ("A&G") expenses and associated overheads are properly assignable to the distribution function because the rate paid by BARC to Old Dominion Electric Cooperative for power supply and transmission

[4] The Commission granted this motion on August 27, 2001.

[5] Staff noted that the Cooperative does not anticipate providing transmission service to customers who shop for energy.

includes a component for A&G expenses. BARC argued that assigning its A&G and overheads to G&T would, in effect, add a second layer of such costs to the generation component. Further, BARC argued that in its role as the local distribution service provider, it is required by the Act to provide default generation service under its capped rates. According to BARC, supplying default generation services provides a benefit available for all consumers on BARC's distribution system, including those consumers who may choose an alternative power supplier. BARC further stated that the responsibility bestowed on it to provide default service is a function of its role as the distribution utility. Thus, the Cooperative urged the Commission to reject Staff's proposal to assign A&G costs to the G&T functions. In the event that the Commission accepts Staff’s proposal, BARC stated that it disagreed with Staff on the proper allocation factor to determine the G&T portion of A&G costs asserting that it was inappropriate to assign such expenditures using an A&G only labor ratio.

With regard to the Staff's recommendations concerning uncollectible expense, customer deposits, and interest on customer deposits, BARC agreed that a portion of these expenses should be attributed to G&T, but took issue with the Staff's method of allocation. BARC also disagreed with the Staff's assignment of load management costs to the G&T function.

In its Response, BARC agreed with the bundled rates proposed on Staff Exhibit Statement 5, with the exception of Schedule LP-2, which the Cooperative requested be corrected to eliminate the $.34 per kW primary discount. BARC further agreed with the total purchased power cost used by Staff, but not with the allocated levels of purchased power cost reflected in the unbundled generation rates proposed by Staff. The Cooperative, therefore, proposed unbundled rates to reflect the allocated purchased power costs and other costs shifted to G&T as proposed by the Cooperative.

On November 9, 2001, the Staff filed a Reply to BARC's comments on the Staff Report.[6] In response to BARC's assertion that certain A&G costs should be allocated to Distribution, the Staff maintained its position that if these costs are shifted to Distribution, rates established for Distribution will subsidize those of G&T, contrary to § 56-590 D of the Code of Virginia, which requires the Commission to set rates that will not result in cost shifting or cross-subsidies between functional units. The Staff also believes that it is appropriate to allocate the payroll and related overheads based on an A&G labor factor, and used a total labor factor to allocate other A&G costs.

The Staff also reiterated its proposal to functionalize a portion of uncollectible expense, customer deposits and interest

[6] On November 14, 2001, the Commission granted Staff's motion requesting leave to file its Reply and provided BARC the opportunity to file any further response on or before November 27, 2001.

on customer deposits, and all costs associated with BARC's load management programs to G&T. In addition, the Staff disagreed with BARC on (i) the proper ratio to use to allocate a portion of uncollectible expense, customer deposits, and interest on customer deposits to G&T, and (ii) the class or classes to which load management costs should be allocated.[7]

BARC filed its Response to the Staff's Reply on November 27, 2001. In its Response, BARC maintained that failure to attribute additional A&G expenses to the generation function does not result in cost-shifting or cross-subsidization of functionally separate units. In addition, BARC urged the Commission to consider its unique statutory obligation to provide default services in Virginia. BARC maintained its position with regard to the inappropriateness of assigning expenditures supporting A&G activities using an A&G only labor ratio. BARC indicated that it would modify its systems as needed to allocate G&T function costs and track those costs. The Cooperative continued to agree with Staff that a portion of uncollectible expense, customer deposits, and interest on customer deposits be assigned to the G&T function, but stated that the ratio used should be based on G&T revenues as a

[7] Staff continued to support the allocated levels of purchased power cost reflected in the unbundled generation rates proposed by Staff. However, in an amendment to its Reply to BARC’s comments filed November 20, 2001, Staff noted that the Cooperative had submitted a revised cost of service study and a proposed modification of the allocation of purchased power costs reflecting the present value billing determinants. Staff stated that BARC’s proposal on the allocation of purchased power costs should be accepted, but that Staff continued to support the allocation of all A&G costs to the G&T function.

percentage of total revenues. With regard to load management costs, the Cooperative maintained its position that 50% of these costs should be considered part of the distribution function.

NOW THE COMMISSION, having considered the Cooperative's application, Staff's Report, the subsequent pleadings, and applicable law, is of the opinion and finds that the application should be approved, subject to the modifications detailed herein.

With respect to the issue of the proper allocation of A&G costs supporting the procurement of wholesale power, we find that the Commission has an obligation pursuant to § 56-590 D of the Code of Virginia to see that no cross-subsidies occur. The function causing the cost should be allocated such costs. A&G costs associated with the procurement of wholesale power support the G&T function, and as such, should not be allocated to the Distribution function. We will, therefore, accept Staff's adjustment allocating certain A&G costs associated with obtaining wholesale power to the Cooperative's G&T function. Further, we accept Staff's functional allocation of labor overheads based on the A&G labor factor.

There are two ways that a cooperative may recover A&G costs associated with the procurement of wholesale power. If a customer remains with the cooperative, the cooperative will recover such costs from the customer. If the customer leaves the cooperative, and the embedded cost of generation exceeds the market, the cooperative will have the opportunity to recover the cost through the wires charge.

We likewise agree with Staff that the allocation factor for uncollectible expense, customer deposits, and interest on customer deposits should be based on each function's relative level of operating expense. We believe this is a reasonable approach in this situation as total G&T expense must be calculated in order to determine the level of G&T revenues, and operating expenses can be used to simulate unbundled revenue.

With regard to the costs for load management, we find that these costs should be fully allocated to G&T and should be allocated across all customer classes, not just the residential class. Load management switches installed for peak shaving are a G&T component because they allow the Cooperative to decrease its power costs by negotiating better rates from the supplier, and the Cooperative would not have load management switches simply for distribution purposes. Further, we agree with Staff that since all customers share in the benefits of lower wholesale power bills, all customers should share the costs, not just the residential class.

We find that G&T costs, as defined in this Order, should be tracked prospectively by the Cooperative in order to ensure accurate functional allocations in any future proceedings before the Commission. We also direct the Cooperative to begin tracking the incremental costs associated with billing and collection costs, as well as the activities that give rise to the customer service and legal and regulatory costs.

Finally, in its cost of service study, BARC discusses the impact of its monthly fuel adjustment factor in relation to the determination of the market price for generation and the wires charge. It is the Cooperative's position that fuel adjustments can be applied monthly without violating §§ 56-582 and 56-583 of the Code of Virginia. We are not persuaded by the Cooperative's argument on this point. However, because it is not necessary that we resolve this issue prior to January 1, 2002, we will defer our consideration of it until next year. In the interim, we direct the Staff to (i) consult with BARC, the other electric cooperatives, and any other interested parties on this issue and (ii) submit a written recommendation to the Commission on or before March 1, 2002, on whether we should implement an annual fuel factor adjustment for the cooperatives in lieu of the current fluctuating monthly fuel charge.

Accordingly, IT IS ORDERED THAT:

(1) BARC's Plan for functional separation pursuant to the Virginia Electric Utility Restructuring Act is hereby approved, subject to the modifications discussed herein.

(2) On or before March 1, 2002, the Staff shall submit a written recommendation to the Commission on whether we should transition to an annual fuel factor adjustment for the

cooperatives from the current fluctuating monthly fuel charge, and if so, how such a transition should occur.

(3) BARC shall provide tariffs, reflecting among other things BARC’s proposed purchased power cost allocation and Staff’s proposal to allocate all A&G costs to the G&T function, and terms and conditions of service to the Division of Energy Regulation that conform to this Order and all applicable Commission Rules and Regulations one hundred fifty (150) days prior to its implementation of retail choice.

(4) This case is hereby dismissed, and the papers shall be placed in the file for ended causes.